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FILED
JAN 18 1946
CHARLES ELMORE CROPLEY

IN THE

Supreme Court of the United States

OCTOBER TERM, 1945

No. 686

LOUIS LOBER,
Petitioner (*Appellant below*),

v.

CANADIAN PACIFIC RAILWAY COMPANY, *et al.*,
Respondents (*Appellees below*).

PETITIONER'S REPLY BRIEF

RALPH ROYALL,
FREDERICK H. STINCHFIELD,
Counsel for Petitioner.

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Canadian's argument begins at page 7 with a headnote which states that: "The Court of Appeals' Decision Must Stand Unless This Court Will Reverse That Court's Interpretation of a Contract." The brief then refers to the holding for the first time made by the Court of Appeals that Articles Fourth and Fifth of the Traffic Agreement do not intend to provide a right of exchange of the 5's for the 4's. We have shown at pages 7 to 9 of our brief that the interpretation of the Court of Appeals is clearly erroneous.

The assumption implied in the above quoted headnote that this Court will not or should not reverse the Court of Appeals upon the interpretation of a contract is baseless. There is no possible reason why an error of the Court of Appeals on such a question of law should not be review-

able here. The Court of Appeals, by injecting such an erroneous determination, could not, we submit, preclude this Court from acting.

Under the heading on page 9 that "The Alleged Conflict of the Present Decision With Previous Decisions of This Court is Non-existent", the brief urges that this Court's decisons upon which we rely are not applicable. The main reason put forward for this is that a long course of mismanagement was not here shown to exist as, for example, in *Taylor* v. *Standard Gas & Electric Co.* That the facts are not the same does not, as respondent so erroneously thinks, make the principle of the decisions inapplicable. The single overreaching abrogation transaction aimed by Canadian directly at the public holders of the 5's for the intended purpose of injuriously affecting the position of these security holders of its subsidiary upon its reorganization to Canadian's own advantage presents a stronger case for subordination than do the cases in which subordination was based upon a long period of mismanagement by the parent of its subsidiary and where the injury to the security holders was not as great or as direct,—or, indeed, was not immediately concerned as here with an ulterior purpose of improperly altering the position of the parties upon a contemplated reorganization.

The above observations apply equally to the decisions in the other circuits which, on the authority of the decisions of this Court, have subordinated the claims of the parent to the claims of the security holders of the subsidiary.

At this point Canadian asserts that, January 1, 1937 having arrived without the 5's having been exchanged for the 4's, the right had expired and Canadian ought not, there-

fore, to be regarded as though standing in the position of a guarantor.

The Respondent is in an oddly inconsistent position in suggesting that the holders of the 5's should have offered their bonds for exchange during the last seven months of 1936. At that time, Canadian claimed, and still claims, that the abrogation agreement, which was made on May 22, 1936, had cancelled the right of the holders of the 5's to offer their bonds for exchange. It seems strange for Canadian to now suggest that, nevertheless, the holders of the 5's should have made the offer during those seven months. Moreover, it is clear that any presentation of bonds during the last seven months of 1936 would have been met with a refusal. It should not be held that the holders of the 5's ought to have done a totally useless act.

When in May, 1936 Canadian abrogated the guaranty agreement, it contemplated having South Shore file the reorganization petition at the end of the year and on January 2, 1937 at ten o'clock A. M. the petition was filed. Considering that Canadian abrogated the exchange agreement some months before its expiration date, it does not stand before the Court in this reorganization proceeding in a position to take advantage of its own wrongful act and claim that the holders of the 5's lost their rights by not presenting their bonds for exchange.

The Court should not permit the abuse of its processes to aid in a final consummation of this overreaching and fraudulent act against the creditors of the debtor in respect of whom Canadian, standing in a fiduciary position, could not deal with the subject in its own interest. The Court was bound to protect the rights of the debtors creditors.

The heading at page 14 states that: "The Suggested Conflict of the Present Decision With New York Law is Non-existent." The brief then cites a decision made by a *nisi prius* judge in New York for the proposition that the holders of the 5's are not donee beneficiaries. We have throughout this proceeding taken the position that the conceptions of Judge Nordbye as to the New York law of third party beneficiaries as shown in that judge's decision in the *McCullogh* case, as well as in the decision made by him herein, are erroneous. The judge classified the holders of the 5's as donee beneficiaries. But, if they are such, it is the settled law of New York that their rights were indefeasible from the beginning and regardless of the insolvency of the promisor, the debtor. Our position has constantly been that the holders of the 5's nevertheless had enforceable legal rights as third party beneficiaries and that these rights were indefeasible at least after the promisor South Shore became insolvent. The authorities referred to at pages 12 to 14 of our brief completely demonstrate the error of the courts below on this aspect of the case.

The heading at page 15 states that: "The Suggested Question As to Whether a Proposed Plan of Reorganization is Fair and Equitable is Not Involved in This Proceeding." The brief at this point admits, at least tacitly, the correctness of the statement at pages 9 and 10 of our petition that the Bondholders Committee has agreed with Canadian to adhere to a proposed Plan that would give the holders of the 5's, in lieu of their bonds and of the interest thereon, which has been fully earned during the nine years while the debtor has been in the hands of the District Court, $500 in face amount of a new 4% income bond, plus $100

in cash in satisfaction of all the rights appertaining to each $1,000 5% First Mortgage Bond now outstanding. Manifestly the existence of this understanding precludes the Bondholders' Committee, which, aside from us, is the only representative of the holders of the 5's in this proceeding, from going forward with the inquiry into the past relations of Canadian and the Debtor, which both of the courts below speak of as pending.

The suggestion which the brief puts forward at this point is that this Court cannot deal with the question here presented until a Plan has been formally promulgated and passed by the Interstate Commerce Commission, the District Court and the vote of the creditors.

The question was properly presented by us for separate trial under Rule 42(b).

A decision of the question of subordination is vital to the intelligent consideration of the basic question of the fairness of any plan of reorganization of this Debtor.

A decision, which we submit should now be made, that the claims of Canadians should be subordinated would furnish the key unlocking the door to a just termination of this proceeding which has been used by Canadian for the purpose of forestalling the rights of the public owners of the securities of this member of Canadian's system of railroads for more than nine years.

A plan of reorganization would then automatically fall into the simple form of giving the holders of the 5's new first mortgage bonds equivalent in face amount to the bonds now outstanding plus the payment in cash out of the earnings of the trusteeship of the interest of which they have so long been deprived,—the debtor's railway and the remaining cash and other current assets to go to Canadian which is the only other interested party.

Broadly viewed such a solution would be eminently just. Canadian has made it plain that it wants to keep the Debtor as a part of its family of railroads. It should be permitted to do so only in recognition of the just rights of these public holders of the Debtor's First Mortgage Bonds.

Respectfully submitted,

RALPH ROYALL,
FREDERICK H. STINCHFIELD,
Counsel for Petitioner.